Before the
Federal Communications Commission
Washington, D.C. 20554

In the Matter of	)	WC 02-147
Motion of Lucent Technologies Inc. For a Declaratory Ruling	) File No.)	

Lucent Technologies Inc.'s Third Supplement
to Petition for Declaratory Ruling

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I. Introduction and Summary

Petitioner hereby updates its declaratory ruling petition concerning a 30-million-plaintiff, nationwide class action lawsuit that collaterally attacks in state court settled determinations of the FCC within its exclusive jurisdiction regarding the detariffing of customer premises equipment (CPE). Although the lawsuit—set for trial August 5, 2002, in an Illinois court—purports to exclusively raise state consumer protection issues, developments in late 2001 make even more clear that many of the claims actually challenge previous FCC orders.

Plaintiffs' recently-filed Third Amended Complaint defines the class to consist solely of "embedded base" customers who leased CPE from January 1, 1984, through at least January 1, 1986. These customers were beneficiaries of an FCC-required and ratified notification program informing them of the FCC's decision to deregulate CPE in light of the competitive nature of the market, and to allow Petitioner to charge market-based CPE rates.[1] Nonetheless, despite contrary findings by the FCC in orders throughout the 1980s, Plaintiffs claim that Petitioner: 1) had, and has, market power in the provision of CPE; 2) was not entitled to set market-based rates for CPE;

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[1] Lucent has operated a leased CPE business since 1996. It has filed this petition on its own behalf and as successor in interest to AT&T Corp., which operated the lease business from 1984 to 1996.

and 3) did not provide sufficient notice in the 1980s to its CPE lease customers to make them reasonably aware of their status as lease customers and their options to purchase, rather than lease, CPE.

Plaintiffs, of course, were permitted to participate in, and appeal, the FCC's CPE detariffing orders. They are not now entitled to yet another bite at the apple. Nor may a state court reexamine the issues the FCC decided 20 years ago, regardless of whether that court ultimately challenges or supports those determinations. If the claims in the underlying lawsuit are allowed to go forward, not only could Petitioner be assessed significant damages for initiating the CPE leasing business in compliance with FCC mandates, but the FCC's jurisdiction and ability to pursue its deregulatory objectives on CPE and other issues could be eroded.

Petitioner does not seek preemption of true consumer protection claims. As the FCC has explained, it did not intend to preempt all state law with its CPE detariffing orders. Petitioner merely asks the FCC to reaffirm its findings: 1) that the CPE market was and is competitive; 2) that Petitioner was and is entitled to set market-based CPE rates and that no state can use "cost-plus" analysis or any similar approach to determine the "correct" price for CPE ; and 3) that the FCC-required and ratified notification campaign was sufficient to make embedded-base customers reasonably aware of their status as lease customers and of their options to purchase CPE.

Failure of the FCC to take such action and preempt state claims that contradict federal findings concerning CPE will have major, long-term ramifications regarding the Commission's ability to successfully implement its statutory directives and policy goals.

II. The Class Action

In 1980, the FCC detariffed CPE in the *Final Decision* of its Second Computer Inquiry and decided that people were no longer to obtain their telephones as part of their basic telephone service on terms subject to state regulation.[2] Instead, consumers were asked to choose either to purchase telephones in the competitive market or to continue to lease their telephones from Petitioner. In setting forth its plan for deregulating embedded CPE provided under tariff in 1983, the FCC made findings regarding market-power, CPE rates, and consumer notification. The FCC determined that its plan ensured that embedded-base customers were given sufficient information to "make informed judgments from a full set of options," as well as "meaningful choices [that] protect[ed] them against dislocations during and after the transition period."[3] The FCC also determined that the market for sold and leased CPE was competitive, concluded that continued rate regulation of CPE would be harmful, and expressly preempted state authority to regulate CPE used in interstate service.[4]

Some thirteen years after the FCC decided these matters, Plaintiffs initiated this litigation in Illinois state court.[5] The lawsuit claims that Petitioner had market power over CPE, at least in part because leased CPE constituted a separate market from sold CPE; that Petitioner should not

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[2] *See In re* Amendment of Section 64.702 of the Commission's Rules and Regulations, *Final Decision*, 77 FCC.2d 384, 388 ¶ 9, 439 ¶ 140, 445 ¶ 156 (1980) (Final Decision).

[3] *See In re* Procedures for Implementing the Detariffing of Customer Premises Equipment and Enhanced Services, *Report and Order*, 95 FCC.2d 1276, 1300 ¶ 36 (1983) (Implementation Order).

[4] *See Final Decision*, 77 FCC.2d at 455-57 ¶¶ 184-189; Computer and Communications Industry Association v. FCC, 693 F.2d 198, 214-16 (D.C. Cir. 1982).

[5] *See* Complaint, Crain v. Lucent Technologies, No. 96-LM-983 (Ill. 3d Jud. Cir. Ct., Madison County) (filed Sept. 5, 1996).

have been allowed to charge market-based rates for leased CPE because the market for CPE was not competitive; and that Petitioner's notices were insufficient to make embedded-base customers aware of their options to purchase or lease CPE.

The Illinois trial court dismissed the complaint in March 1999 on the grounds that the FCC's CPE detariffing regime preempted Plaintiffs' claims.[6] In April 1999, however, Plaintiffs filed a motion to reconsider that decision.[7]

While the trial court was considering this motion, the FCC filed an *amicus* memorandum. The FCC memorandum emphasized that "it [took] no position on the merits of the claims, or even on whether the laws invoked by the plaintiffs apply to the sale or lease of CPE."[8] The FCC memorandum explained that the FCC had not intended to preempt all state contract and consumer protection law, but that it had preempted state law that is inconsistent with the FCC's deregulatory regime, such as utility-type regulation of CPE.[9]

Upon the filing of the FCC *amicus* memorandum, Petitioner sought additional guidance from the FCC by petitioning for a declaratory ruling that clarifies the preemptive scope of the FCC CPE detariffing decisions.[10] Petitioner twice supplemented the request.[11] The FCC has not

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[6] *See* Order, Crain v. Lucent Technologies, No. 96-LM-983, at 2-4 (Ill. 3d Jud. Cir. Ct., Madison County Mar. 10, 1999) (Dismissal Order).

[7] Plaintiffs' Motion for Reconsideration, Crain v. Lucent Technologies, No. 96-LM-983 (Ill. 3d Jud. Cir. Ct., Madison County) (filed Apr. 8, 1999).

[8] Memorandum of FCC as *Amicus Curiae*, Crain v. Lucent Technologies, No. 96-LM-983, at 3 (Ill. 3d Jud. Cir. Ct., Madison County) (filed May 24, 1999) (FCC *Amicus* Memorandum).

[9] *Id.* at 2-3.

[10] *See* Motion of AT&T Corp. and Lucent Technologies Inc. for Declaratory Ruling (filed May 24, 1999).

[11] Petitioner filed supplements on June 16, 1999, and December 10, 1999. Petitioner files this Third Supplement to further update the record.

yet acted.

The Illinois trial court reinstated the complaint in July 1999,[12] apparently interpreting the FCC *amicus* memorandum to mean that any claims under color of state consumer protection law are not preempted, even if those claims ask the trial court to make findings contradicting or overruling previous FCC findings of fact and conclusions of law. The reinstatement was affirmed by an intermediate state appellate court.[13] The FCC did not participate in the appeal.

Since the FCC filed its *amicus* memorandum, and during the past several months, events in the underlying litigation have necessitated Petitioner's filing of this supplement to its pending request for declaratory ruling. On Nov. 5, 2001, Plaintiffs filed a Third Amended Complaint that limited the class to the embedded-base customers who were the subject of the FCC CPE detariffing orders.[14] In addition, from late 2001 to early 2002, Plaintiffs detailed in reports and depositions, some of which are attached to this Third Supplement, the precise bases for their allegations. The new submissions demonstrate that much of Plaintiffs' lawsuit is rooted in claims regarding market definition, market-power, the cost basis for CPE rates, and consumer notification. These claims ask the state court to contradict prior FCC findings of fact and conclusions of law.

Petitioner's regulatory expert, Albert Halprin, was deposed in April 2002. As he explains in his attached expert report, the lawsuit asks the state court to engage in precisely the kind of

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[12] *See* Order, Crain v. Lucent Technologies, No. 96-LM-983 (Ill. 3d Jud. Cir. Ct., Madison County July 2, 1999).

[13] Crain v. Lucent Technologies, 739 N.E.2d 639 (Ill. App. Ct. 2000), *petition for leave to appeal denied*, 747 N.E.2d 352 (Ill. 2001).

[14] *See* Third Amended Complaint, Sparks v. AT&T Corp., No. 96-LM-983 (Ill. 3d Jud. Cir. Ct., Madison County) (filed Nov. 5, 2001).

utility-type analysis and regulation that the FCC said it preempted. Indeed, several of the claims ask the court to reconsider and reverse decisions reached by the FCC. The lawsuit thus would directly frustrate the FCC's deregulatory regime for CPE.[15]

III. Many of Plaintiffs' Claims Contradict—and Thus are Preempted by—FCC Findings of Fact and Conclusions of Law

Plaintiffs base their claims on past action or inaction by Petitioner that the FCC ratified during the implementation of the CPE transition, or on the existence of market power that the FCC has already ruled Petitioner lacks. These claims are "at odds with" the FCC's CPE detariffing orders, and as such should be preempted.

The FCC *amicus* memorandum is fully consistent with what Petitioner seeks. The memorandum states that "[t]o the extent that [state laws] would apply generally to the sale or lease of CPE by companies other than telephone companies, ... the FCC has not preempted their application to the telephone companies."[16] The FCC made clear, however, that it had

> decided to preempt the states from regulating ... "to the extent that their terminal equipment regulation is at odds with the regulatory scheme we have set forth." That regulatory scheme "essentially involves the removal of traditional utility type regulation over CPE, and the requirement that if carriers of the Bell System choose to provide CPE, they do so pursuant to the structure we have prescribed."
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> The Commission thus declared that "utility regulation of CPE is contrary to the national public interest" and that states may not impose such regulation.[17]

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[15] *See* Halprin Report at 3-4 (concluding "that AT&T's actions, which are the subject of this lawsuit, clearly could have been anticipated by regulators and the marketplace, were in fact anticipated, and were lawful and appropriate. Moreover, both the prayer for relief and the measures that the plaintiffs and their experts insist should have been in place add up to nothing more than an unwarranted attempt to retroactively re-regulate the CPE marketplace. Such measures are inconsistent with, and would violate, both the letter and spirit of the FCC's rules and orders").

[16] *FCC Amicus Memorandum*, at 3.

[17] *Id.* at 2-3 (quoting *In re* Matter of Amendment of Section 64.702 of the Commission's Rules and Regulations, *Memorandum Opinion and Order*, 84 FCC.2d 50, 103 ¶ 154 (1980) (Reconsideration Order), *Memorandum Opinion and Order on Further*

Indeed, in filing its *amicus* memorandum, the FCC did not question the Illinois trial court's initial determination that "the Commission's program of transition to deregulation had required certain steps by AT&T (and eventually by Lucent Technologies, Inc.) that could not be challenged in a state lawsuit arising from conduct that occurred during the transition period."[18] Rather, the FCC merely questioned the trial court's broader finding that application of state consumer protection law to any conduct in connection with Petitioner's CPE offerings was completely foreclosed.[19]

Plaintiffs' claims based on market power, CPE rates, and consumer notification are "at odds with" FCC directives and would require the state court to revisit (and impose additional obligations regarding) the FCC's detariffing process. Consequently, these claims are preempted.

A. The FCC Has Held that Petitioner Lacks Market Power Over CPE and Has No Special Duties Different From Those of Any Other CPE Vendor

The FCC has already found that Petitioner's "CPE operations in recent years have been, and for the foreseeable future will be, very much susceptible to competition," and thus the FCC has already disposed of Plaintiffs' claims that the leased and sold CPE businesses are in separate markets and that Petitioner has market power.[20] As noted by the FCC, the "competitive

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Reconsideration, 88 FCC.2d 512, 523 ¶ 33, 541 n.34 (1981) (Further Reconsideration Order) (emphasis added)).

[18] Reply of FCC in Support of its Motion for Leave to File Memorandum as *Amicus Curiae*, Crain v. Lucent Technologies, No. 96-LM-983, at 3-4 (Ill. 3d Jud. Cir. Ct., Madison County) (filed June 11, 1999).

[19] *Id.* at 4.

[20] *Implementation Order*, 95 FCC.2d at 1298 ¶ 34. *See also id.* at 1320-22 ¶¶ 69-70; *Final Decision*, 77 FCC.2d at 440 ¶ 143, 452 ¶ 174, 454 ¶ 179. Although the FCC initially required AT&T to operate its CPE business out of a separate subsidiary, it did so out of concern that AT&T might leverage its strengths from other markets or other services, not because AT&T had any monopoly power over the CPE market itself. *See Final Decision*, 77 FCC.2d at 388-89 ¶ 12, 452 ¶ 174 & n.64, 453 ¶ 177; *Reconsideration Order*, 84 FCC.2d at 72 ¶ 65.

marketplace offers ready relief to those residential users who may not wish to continue leasing equipment."[21] Consequently, the FCC ruled that Petitioner "should have the same regulatory status in marketing CPE as any other equipment vendor."[22] As the FCC *amicus* memorandum explains, "if [generally applicable state consumer protection and contract laws] would apply to non-telephone company vendors of CPE, they should apply equally to AT&T and Lucent."[23] Thus, Petitioner has no special duties and is "free to operate as any new business enterprise in the competitive provision of CPE,"[24] even though it gained its CPE lease customers as a result of divestiture and the CPE detariffing orders.

The foundation for most of Plaintiffs' claims, however, is that Petitioner had, and has, a special duty to embedded-base customers that requires it to operate its business differently from companies operating in a competitive market. According to Plaintiffs, these special duties arise because petitioner allegedly had market power over CPE and because petitioner "inherited" its customers as part of the divestiture decree and the CPE detariffing orders.[25] Indeed, Plaintiffs go so far as to claim Petitioner has a special duty to inform customers of alternative CPE options. This is plainly inconsistent with the FCC's orders, and as such must be preempted. The FCC, not a state court, has jurisdiction to determine whether Petitioner has market power over CPE or special obligations to its divestiture-era customers. That decision is not subject to any type of

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21 *Implementation Order*, 95 FCC.2d at 1325 ¶ 77.

22 *See Final Decision*, 77 FCC.2d at 446 ¶ 159.

23 *FCC Amicus Memorandum*, at 7 (emphasis added).

24 *Further Reconsideration Order*, 88 FCC.2d at 529 ¶ 47.

25 *See, e.g.*, TerKeurst Report at 1-5, 7, 14 (Nov. 2, 2001) (claiming Petitioner has additional duties because of "widespread confusion following divestiture").

state review. This is true whether the state action purports to address the single national market found by the FCC or a "unique" market within one or more individual states.

B. The FCC Has Held That Petitioner, Like Any Other CPE Vendor, is Entitled to Charge Market-Based Rates

Because the FCC determined that Petitioner lacked market power over CPE and that the CPE market was competitive, the FCC concluded that continued rate regulation of Petitioner's CPE would harm competition and innovation.[26] Indeed, the FCC *amicus* memorandum explicitly states that the Illinois state court's order dismissing Plaintiffs' complaint "correctly determined that the FCC, in its detariffing decision, 'intended to rely on the forces of the market to act as a regulatory tool in the future.'"[27]

As far back as 1980, the FCC said that "according broad discretion to carriers to raise or lower terminal equipment rates ... is not likely to result in users being charged unreasonable or unreasonably discriminatory rates."[28] In fact, the FCC concluded that "given the degree of competition in this market some individualized negotiations among terminal equipment providers and customers will result in more vigorous and effective competition .... There may be even less of a danger of unreasonable or unreasonably discriminatory rates when customers are in a position to 'comparison shop.'"[29] Thus, the FCC determined that Petitioner, like any CPE vendor, was entitled to charge market-based rates.

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[26] *See Final Decision*, 77 FCC.2d at 388 ¶ 9, 440-41 ¶¶ 143-45, 446 ¶ 159; *Reconsideration Order*, 84 FCC.2d at 65 ¶ 46; *Implementation Order*, 95 FCC.2d at 1280 ¶ 3, 1301 ¶ 38.

[27] *FCC Amicus Memorandum*, at 7 (quoting *Dismissal Order*, at 2).

[28] *See Final Decision*, 77 FCC.2d at 455 ¶ 183.

[29] *Id.* at 455 n.69.

Consequently, the FCC ceased federal rate regulation of CPE, and preempted state utility-type rate regulation of CPE, regardless of the form.[30] Indeed, the FCC explicitly stated that it was "aware that requiring carriers to unbundle and detariff CPE used jointly in the provision of interstate and intrastate service has the practical effect of eviscerating state jurisdiction to establish charges for this terminal equipment in a manner that conflicts with federal interests."[31]

This is not to say that Petitioner's CPE rates are necessarily beyond reproach. The FCC has said that "under our ancillary jurisdiction, we have the authority to rule on questions of whether [Petitioner's] actions violate the Communications Act or our previous orders."[32] Thus, the FCC has jurisdiction to determine if CPE rates violate the Communications Act.

Plaintiffs claim that as a result of Petitioner's supposed "market power," Petitioner had special obligations to charge a price below what customers were willing to pay.[33] They claim Petitioner's rates violated state consumer protection law even if customers were not deceived in any way.[34] They ask the state court to engage in a utility-type "cost-plus reasonable rate of return"

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[30] *Id.* at 455-57 ¶¶ 184-189; Computer and Communications Industry Association v. FCC, 693 F.2d 198, 214-16 (D.C. Cir. 1982).

[31] *Reconsideration Order*, 84 FCC.2d at 103 ¶ 154.

[32] *See In re* Procedures for Implementing the Detariffing of Customer Premises Equipment and Enhanced Services, *Memorandum Opinion and Order*, 100 FCC.2d 1298, 1307 ¶ 16 (1985). *See also Final Decision*, 77 FCC.2d at 451-52 ¶¶ 172-74 & n.64.

[33] *See, e.g.,* Cameron Deposition at 57-59, 66 (Nov. 6, 2001) (arguing Petitioner could not "charge the maximum the market will bear" because petitioner has "market power" and "consumers don't have the alternatives that you might otherwise think they have").

[34] *See, e.g., Plaintiffs Memorandum in Support of Motion for Nationwide Class Certification*, at 6-7 (filed June 25, 2001) (arguing that "an unconscionably high price alone is unlawful," that "[a]n unconscionable price by itself *is* ... an actionable violation of the New Jersey [Consumer Fraud Act]," and that unconscionability exists where price is "excessive in relation to defendant's cost"); Alexander Deposition at 273-77 (Jan. 8, 2002) (claiming "prices became exorbitant and thereby unconscionable [when] the company ... priced its lease charges on the theory of what the market would bear").

analysis to set an "appropriate" charge.[35] In fact, they ask the court to make determinations regarding such traditionally regulatory matters as recovery of direct and fully distributed costs, and set forth capital recovery schedules.[36] They claim that the interim rates established by the FCC for the two-year transition period only should have been adjusted over the past 16 years for inflation.[37] Thus, according to Plaintiffs, Petitioner should grant refunds to all class members.

To allow claims that market-based rates are excessive under state consumer protection laws is tantamount to allowing the utility-type rate regulation of CPE that the FCC preempted. This would interfere with the FCC's deregulatory policy, which is designed to encourage competition and innovation in the market for CPE used in connection with interstate service. Plaintiffs' claims that Petitioner's rates have been "too high" and that the "excess amount" should be returned to customers ask the Illinois trial court to engage in precisely the kind of utility-type rate regulation that the FCC explicitly chose to preempt. This is true even though the FCC is not actively regulating Petitioner's CPE rates. The FCC's decision to leave rates unregulated is itself entitled to preemptive effect because it was a reasoned determination that rate regulation of CPE is inappropriate and that the market should govern.[38]

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[35] *See, e.g.,* Cameron and Kahn Disclosure Statement, at 51 (October 8, 2001) (declaring that Petitioner's prices are not reasonable because they were not based "on the cost of providing the equipment and service plus a reasonable profit" and stating that a reasonable rate should be established based on the "regulated rate of return approach"); Cameron Deposition at 14, 38, 49, 51 (testifying that she was retained to perform "reasonable cost price estimates" for leased CPE and to "estimate the reasonable cost-based price for these sets," that Petitioner's lease prices were too high because they "do not reflect a reasonable set of costs," and that she was attempting to determine "what would a regulator have allowed" petitioner to charge).

[36] *See, e.g.,* Cameron and Kahn Disclosure Statement at 51.

[37] *Id.* at 51 (calculating reasonable rate "based on lease rates charged during the transition period" plus "a general rate of inflation").

[38] *See* Computer and Communications Industry Association v. FCC, 693 F.2d 198, 217 (D.C. Cir. 1982). *Cf.* AT&T v. *City of Portland,* 216 F.3d 871, 879 (stating that "the FCC

C. The FCC-Required and Ratified Notification Program Was Sufficient to Make Consumers Reasonably Aware of Their Status as Lease Customers and Their Options to Buy CPE

The FCC determined the appropriate level of notification that Petitioner should provide to embedded-base customers.[39] To ensure customers were reasonably aware of their status as lease customers of Petitioner and of their options to purchase CPE, the FCC required Petitioner to notify all embedded CPE customers of their right "to buy or continue to lease [Petitioner's] equipment" or to "terminate lease service and obtain equipment from other vendors."[40] Further, the FCC required Petitioner to inform customers that they need not obtain their telephones from Petitioner to continue receiving dial-tone service.[41] The FCC also found that Petitioner's written notifications, combined with competition from retail suppliers, the new sale programs of existing suppliers, and a twelve million dollar national advertising program, would "aid[] customers in making informed choices regarding their telephone equipment."[42]

The FCC required Petitioner to poll its customers in 1983 using a "modified negative option," whereby people were asked to indicate whether they wished to continue leasing their CPE or to end that arrangement and buy a telephone.[43] The FCC specifically prohibited Petitioner, however, from mentioning what would happen if customers failed to indicate a

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has broad authority to forbear from enforcing the telecommunications provisions if it determines that such action is unnecessary to prevent discrimination and protect consumers, and is consistent with the public interest").

39 *See* Halprin Deposition at 237-239.

40 *Implementation Order*, 95 FCC.2d at 1352 ¶ 125 n.107.

41 *Id.* at 1354 ¶ 131.

42 *Id.* at 1321 ¶ 69.

43 *Id.* at 1320 ¶ 67.

choice.[44] If, a person did not send in a ballot, the FCC directed Petitioner to treat those customers as selecting the lease option.[45]

The FCC did not require Petitioner to repeat the balloting during or after the transition period, or to provide any additional notification. Although some parties, including state regulators, asked the FCC to grant them the power to require additional notices or sale options, the FCC refused to do so.[46] In fact, the FCC specifically stated that after the transition period, Petitioner's lease business should be detariffed and Petitioner would, as a result, have no special notification obligations different than any other CPE vendor.[47] The FCC said that to require otherwise would harm competition and innovation.[48]

Plaintiffs do not question that the notification took place pursuant to FCC order, and Petitioner notes that the FCC in fact monitored Petitioner's compliance with its orders.[49] Rather, Plaintiffs claim that the FCC-required and ratified notification program was misleading and inadequate because it: a) did not explain to customers that they were leasing telephones from Petitioner; b) did not explain that customers could terminate their CPE leases without losing local telephone service; c) did not inform people that they had a choice to stop leasing; and d) did

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[44] *See* Halprin Report at 19-21.

[45] *Implementation Order*, 95 FCC.2d at 1320 ¶ 67.

[46] *See id.* at 1302-05 ¶¶ 41-44, 1322 ¶ 71.

[47] *See Final Decision*, 77 FCC.2d at 446 ¶ 158.

[48] *See id.*

[49] *See Implementation Order*, 95 FCC.2d at 1291 ¶ 21 (concluding that FCC's "statutory powers will enable us to monitor AT&T's compliance with our requirements and to take any necessary remedial action in the event of non-compliance"); Halprin Report at 2 (stating that "AT&T's actions ... were for some time monitored for compliance by the FCC itself"); Halprin Deposition at 356 (testifying that the FCC "monitored, cared about the progress of CPE deregulation and required AT&T to make ... reports and ... they were made").

not inform customers that if they failed to respond to the campaign survey they would remain lease customers.[50]

In actuality, the FCC-required and ratified program did provide most, if not all, of this information, and some of the information that was not provided was not provided at the direction of the FCC, as in the case of the "modified negative option." Yet now, almost 20 years later, Plaintiffs' rely on the FCC-required omission and resulting treatment of certain consumers as lease customers as the basis for their claim of consumer fraud.[51] They claim that because Petitioner inherited its customers through the negative option established in the FCC's detariffing program, petitioner has notification obligations beyond those imposed upon other companies,[52] despite the FCC's holding to the contrary.

In ratifying Petitioner's notification procedures, the FCC determined that the notification campaign would provide sufficient notice to make consumers reasonably aware of their status as

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[50] *See* TerKeurst Report at 4, 14 (claiming that "some customers do not know they are leasing;" that customers do not know "their leased phone can be replaced by a purchased one;" that customers do not know how "to terminate a lease;" that due to "widespread confusion following divestiture," customers do not understand "the services and responsibilities of AT&T and the local telephone company;" and that the FCC-required and approved notification to the class "was misleading and deceptive in several respects").

[51] *See, e.g.,* Alexander Report at 6 (Oct. 23, 2001) (claiming "what made [petitioner's] scheme even worse is that these customers never affirmatively entered into these transactions" ... "at the end of the transition period"); TerKeurst Report at 7 (alleging Petitioner took advantage of divestiture-era customers because the lease program "was set up as a negative option, i.e., AT&T assumed when the embedded lease business was transferred upon divestiture that a customer wanted to continue leasing the telephone unless the customer took active steps to *stop leasing*").

[52] *See, e.g.,* TerKeurst Report at 1-5, 7, 14 (claiming Petitioner took advantage of customers based on (a) "widespread confusion following divestiture," (b) the fact that "customers 'inherited' their leases from monopoly days," (c) the lease program being "set up as a negative option," and (d) "the notice that AT&T sent in 1983 to inform customers that their leases were being transferred to AT&T [being] misleading and deceptive in several respects").

lease customers and their options to purchase CPE.[53] Indeed, the FCC required Petitioner "to provide the customer with all CPE-related information necessary or useful for facilitating the customer's opportunity to seek alternative providers of CPE."[54] To suggest that the FCC-ratified notification was inadequate or should have been supplemented is to challenge the FCC's determination of what was "necessary or useful." To hold Petitioner liable for following an FCC-mandate or for not repeating balloting when the FCC decided that it was not necessary would upset the balance the FCC struck.[55]

Plaintiffs or anyone acting on their behalf, like all interested parties, could have brought their claims to the FCC at the time or subsequently. They cannot now challenge the FCC's determinations by claiming that state law makes such federally mandated and supervised actions unlawful. A state court cannot consider whether the notifications were insufficient, whether additional notification should have been provided, or whether the notification that was provided met the FCC's requirements. Such determinations are within the jurisdiction of the FCC, not a state court. Thus, any challenge to the notification campaign is clearly preempted, as is any claim that after the transition period Petitioner had or has any notice obligation that is different than those of any other CPE vendor.

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[53] *See Implementation Order*, 95 FCC.2d at 1292 ¶ 21 ("accept[ing] AT&T's proposed sale and lease program for residence and business single-line CPE, finding that the proposal [was] consistent with [FCC] objectives in this proceeding" and requiring AT&T "to comply with this program"). *See also id.* at 1301 ¶ 38, 1321 ¶ 69.

[54] *Id.* at 1352 ¶ 125 (emphasis added).

[55] *See Id.* at 1318 ¶ 65.

IV. The FCC Should Expeditiously Issue a Declaratory Ruling Reaffirming its Findings of Fact and Conclusions of Law in the CPE Detariffing Proceeding

In light of new developments in the case, the looming August 5, 2002, trial date, the Plaintiffs' mischaracterization of the FCC's position, and the trial court's apparent misunderstanding of the FCC's *amicus* memorandum, Petitioner asks the FCC to expeditiously issue a declaratory ruling reaffirming its prior findings of fact and law that:

1. (a) the CPE lease and sale businesses comprise one market; (b) Petitioner had and has no market power over CPE and owed or owes customers no special duties different from those of any other CPE vendor, notwithstanding its inheritance of the embedded base through a "negative option;" (c) the CPE business was and is competitive; and (d) states are preempted from determining whether Petitioner had or has market power or special duties regarding CPE, or whether the CPE market was or is competitive;

2. (a) Petitioner, notwithstanding its inheritance of the embedded base through a "negative option," had and has no special pricing obligations, and was and is entitled to set rates based on what its customers were willing to pay; and (b) states are preempted from engaging in utility-type rate regulation to determine "reasonable" charges based on cost-price estimating, the prices set by the FCC during the transition period (adjusted for inflation), or an analysis of Petitioner's costs or expenses plus a reasonable profit, in the context of a lawsuit claiming that, under state consumer protection laws, Petitioner's lease rates were unconscionable because they were based on what customers were willing to pay;

3. (a) embedded-base customers who leased CPE between January 1, 1984, and January 1, 1986, were provided with all legally required information regarding the lease service and their options to purchase CPE; (b) embedded-base customers were provided sufficient information to be reasonably aware of their status as leased CPE customers; (c) embedded-base customers were provided sufficient information from which they could decide whether to purchase CPE; (d) Petitioner, notwithstanding its inheritance of the embedded base through a "negative option," like all CPE vendors, had and has no further obligation to provide additional notification regarding alternatives to leasing; and (e) that states may not determine whether previous notifications by Petitioner were or are sufficient or whether additional notifications regarding customer options were required after the transition period; and

4. (a) any claim that asks a trial court to make findings contrary to those previously made by the FCC or that is based upon circumstances created by FCC action (such as the Petitioner's inheritance of embedded-base customers through a "negative option" or Petitioner's status as the CPE provider to embedded-base customers

after divestiture), is outside the scope of state consideration, even when raised under the color of state consumer protection law; and (b) pricing and notification claims based on such factors must be pursued as allowed under the Communications Act.

In the alternative, if these prior FCC determinations need review, or if there is a question as to whether Petitioner met its obligations under the prior FCC orders, Petitioner asks the FCC to exercise its continuing, primary jurisdiction over CPE to consider these issues.

The FCC action Petitioner requests is appropriate. Indeed, at the time of detariffing, the FCC said that it would "assess ... the legality under the Communications Act of future attempts by the states to regulate CPE ... on an *ad hoc* basis."[56] Petitioner is not asking the FCC to hold that legitimate state consumer fraud claims are preempted. However, state claims based upon the "special" nature of embedded-base customers, or supposed "special" obligations of Petitioner as the FCC-mandated embedded-base supplier, are outside the scope of any state consideration.

V. Conclusion

Telephone leasing is not a business Petitioner chose to enter. The FCC directed Petitioner to lease CPE as part of the FCC's overall decision to further the public interest through a transition to a competitive market for telephone equipment. Petitioner conducted that business in a manner fully consistent with the FCC's instructions and subject to FCC authority and reporting requirements. It is inappropriate now to expose Petitioner to a potential damages award for following that mandate, to allow a state court to reopen the very issues the FCC resolved from 1980 to 1986, or to allow a state court to determine whether Petitioner met its obligations under the FCC-required and ratified program. Plaintiffs should not be allowed to ask a state court to

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[56] *Reconsideration Order*, 84 FCC.2d at 103 ¶ 154.

undertake, even in the context of a lawsuit purporting to raise state consumer protection claims, utility-type regulation that the FCC has preempted states from otherwise imposing.

Allowing these claims to continue in an Illinois court will do more than unjustly harm Petitioner, however. Should the case continue on its present course, it will infect the CPE market with uncertainty by allowing each state to reopen issues long-ago laid to rest by the FCC, and it will do so at a time when market certainty is desperately needed. It could also set dangerous precedent that encroaches on the FCC's jurisdiction and undermines the FCC's deregulatory goals, not just regarding CPE, but regarding other issues as well, such as broadband deployment. Regardless of whether the state court reaches the same conclusions that the FCC did, simply allowing these claims to proceed suggests that state courts have jurisdiction to reconsider FCC findings in areas of telecommunications policy that the FCC chose to preempt.

If the FCC does not intercede now—when Pandora's box can be closed by a declaratory ruling in which the FCC merely reaffirms its previous findings as applied to particular claims by Plaintiffs—the FCC may face a much larger drain on its resources and a range of problems far more difficult to resolve. This class action is but one of six pending in state courts nationwide. If the FCC does not act now to protect its preemptive authority and primary jurisdiction, the FCC may need to intervene in appeals of those decisions as they spin out of control. Moreover, many other plaintiffs will be encouraged to file similar suits, in the CPE context or others.

For these reasons, Petitioner asks the FCC to grant the declaratory ruling it seeks in this petition.

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CERTIFICATE OF SERVICE

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